

ST 07-16

Tax Type: Sales Tax

Issue: Responsible Corporate Officer – Failure to File or Pay Tax

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS**

THE DEPARTMENT OF REVENUE)	No.	00-ST-0000
OF THE STATE OF ILLINOIS)	IBT No.	0000-0000
v.)	NPL Nos.	0000-000-0000
JOHN DOE & SMITH JONES,)		0000-000-0000
as responsible officers/employees of ABC, Inc.)		
d/b/a Anywhere ABC,)	John E. White,	
Taxpayer)	Administrative Law Judge	

RECOMMENDATION FOR DISPOSITION

Appearances: Scott Schimanski, Law Offices of Thomas W. Lynch, P.C., appeared for John Doe and Smith Jones; Marc Muchin, Special Assistant Attorney General, appeared for the Illinois Department of Revenue.

Synopsis:

This matter arose when John Doe (John Doe) and Smith Jones (SJones) (collectively, taxpayers), protested the Notice of Penalty Liability (NPLs) the Illinois Department of Revenue (Department) issued to each as a responsible officer of ABC, Inc., d/b/a Anywhere ABC (ABC). Each of the NPLs assessed a penalty equal to ABC's unpaid Retailers' Occupation Tax (ROT) liabilities for transactions performed during the months of June 1999 through February 2000, but not inclusive. The penalties assessed against each taxpayer was a personal liability penalty, issued pursuant to § 3-7 of Illinois' Uniform Penalty and Interest Act (UPIA).

John Doe and SJones each testified at Hearing, and they also offered the testimony of a Department employee, as well as documentary evidence. I have reviewed that evidence, and I am including in this recommendation findings of fact and

conclusions of law. I recommend that the NPLs be finalized after being revised as described in this recommendation.

Findings of Fact:

1. ABC was an Illinois corporation that sold motor vehicles at retail. *See* Department Exs. 1-2 (ABC of NPLs).
2. John Doe and SJones were each principles of ABC, and each had the responsibility for filing returns for ABC and for paying the taxes required to be shown due on those returns. Hearing Transcript (Tr.) pp. 85-87 (SJones), 111-12, 114 (John Doe).
3. On June 5, 1999, ABC sold a 1999 Isuzu Rodeo LS 4dr, bearing a VIN of 000000000000000000, to Auto Lease, Inc. (hereinafter, GE CAL). Taxpayer Exs. 1, 9. ABC prepared and filed an ST-556 return with the Department regarding its June 5, 1999 sale to GE CAL (hereinafter, the 6/5/99 sale), and the Department processed that return on the 211th day of 1999. Taxpayer Ex. 9 (copy of the ST-556 return ABC filed regarding the 6/5/99 sale); *see also* Tr. pp. 20-21, 25, 29, 32-33, 35 (testimony of Department employee James Barborka (Barborka), describing the significance of batch numbers stamped onto ST-556 returns when received by the Department).
4. Following ABC's 6/5/99 sale, an application for an original Illinois title for the vehicle was filed, and the transaction number printed on the ST-556 that ABC filed regarding that 6/5/99 sale was entered onto the original title application. Taxpayer Ex. 11 (certified copy of application for title for the vehicle that was the subject of the 6/5/99 sale).
5. On October 2, 1999, ABC sold a 1999 Isuzu Rodeo LS 2dr, bearing a VIN of 000000000000000000, to GE CAL. Taxpayer Ex. 8 (copy of the ST-556 return ABC

filed regarding the 10/2/99 sale). ABC prepared and filed an ST-556 return with the Department regarding that 10/2/99 sale, and the Department processed that return on the 18th day of 2000. *Id.*

6. Following ABC's 10/2/99 sale, an application for an original Illinois title for the vehicle was filed, and the transaction number printed on the ST-556 that ABC filed regarding that 10/2/99 sale was entered onto the original title application. Taxpayer Ex. 12 (certified copy of application for title for the vehicle that was the subject of the 10/2/99 sale).
7. On November 6, 1999, ABC sold a 1999 Isuzu Rodeo, bearing a VIN of 000000000000000000, to G.E. Capital Auto Financial, Inc. (hereinafter, GE CAF). Taxpayer Ex. 7 (copy of the ST-556 return ABC filed regarding the 11/6/99 sale). ABC prepared and filed an ST-556 return with the Department regarding that 11/6/99 sale, and the Department processed that return on or about the 86th day of 2000. *Id.*
8. Following ABC's 11/6/99 sale, an application for an original Illinois title for the vehicle was filed, and the transaction number printed on the ST-556 that ABC filed regarding that 11/6/99 sale was entered onto the original title application. Taxpayer Ex. 13 (certified copy of application for title for the vehicle that was the subject of the 11/6/99 sale).
9. On February 28, 2000, ABC sold a 1999 Isuzu Trooper, bearing a VIN of 000000000000000000, to GE CAL. Taxpayer Ex. 6 (copy of the ST-556 return ABC filed regarding the 2/28/00 sale). ABC prepared and filed an ST-556 return with the Department regarding that transaction, and the Department processed that return on the 146th day of 2000. *Id.*

10. Following ABC's 2/28/00 sale, an application for an Illinois title for the vehicle was filed, and the transaction number printed on the ST-556 that ABC filed regarding that 2/28/00 sale was entered onto the title application. Taxpayer Ex. 14 (certified copy of application for title for the vehicle that was the subject of the 2/28/00 sale).
11. On each of the ST-556 returns ABC filed regarding its 6/5/99, 10/2/99, and 2/28/00 sales to GE CAL, and its 11/6/99 sale to GE CAF, ABC reported no tax due because the value of the vehicle(s) it took in trade regarding those transactions exceeded the selling price of the new vehicle that was being purchased by either GE CAL or by GE CAF, as lessors. Taxpayer Exs. 6-9.
12. Doe and SJones sold their interest in ABC in 2002. Tr. pp. 86 (SJones), 111-12 (John Doe).
13. An ST-556 return consists of a three-page formset, which includes a separate and differently colored page to be retained by the Department, by the retailer, and by the purchaser. *See* Taxpayer Exs. 1-5 (ABC of purchaser's ABC of ST-556 returns); Taxpayer Exs. 6-9 (ABC of Department's ABC of ST-556 returns); 86 Ill. Admin. Code § 130.540 (Illinois Retailers Occupation Tax regulation titled, "Returns on a Transaction by Transaction Basis").
14. Each ST-556 return includes a unique transaction number. 86 Ill. Admin. Code § 130.540(b); Taxpayer Exs. 1-5; Taxpayer Exs. 6-9.
15. The Department issued an NPL to each taxpayer on September 6, 2005. Department Exs. 1-2.
16. On each of the NPLs, the Department provided the following information to identify the assessments the Department determined was due from, and remained unpaid by,

ABC:

Assessment number, tax type, and period covered	Tax	Penalty	Interest	Total liability
000000000000000000 ROT/UT 1999/06	\$3.00	\$2.00	\$3.36	\$8.36
000000000000000000 ROT/UT 1999/06	\$0.00	\$250.00	\$50.92	\$300.92
000000000000000000 ROT/UT 1999/06	\$0.00	\$250.00	\$96.79	\$346.79
000000000000000000 ROT/UT 1999/06	\$147.00	\$64.00	\$144.78	\$355.78
000000000000000000 ROT/UT 1999/10	\$0.00	\$0.00	\$487.01	\$487.01
000000000000000000 ROT/UT 1999/11	\$2,439.00	\$940.00	\$1,917.80	\$5,296.80
000000000000000000 ROT/UT 2000/02	\$1,576.00	\$694.00	\$1,318.48	\$3,588.48
Sum of total liability				\$10,384.14

Department Exs. 1-2 (cABCes of, respectively, the NPLs issued to SJones and Bounoauo).

17. Five of the seven assessments identified within the NPLs arose as a result of the Department's receipt of, and actions regarding, purchaser's ABC of ST-556 returns that the Department obtained from someone other than ABC. Taxpayer Exs. 1-5 (ABC of purchaser's ABC of ST-556 returns); Tr. pp. 19, 21, 80-84 (Barborka). For convenience, I shall refer to these purchaser's ABC of returns as 3d party returns.

18. No evidence was introduced to show how the remaining two assessments identified on the NPLs (i.e., assessment numbers 000000000000000000 and 000000000000000000) arose, and/or the bases therefore.

19. The Department obtained the 3d party returns years after the transactions reflected on those 3d party returns occurred. Taxpayer Exs. 1-5 (processing/batch number stamped onto each exhibit reflect the Department's processing of them in 2003 and 2004); Tr.

pp. 20-21, 25, 29, 32-33, 35 (Barborka).

20. Four of the five assessments identified within the NPLs involve ABC's 6/5/99, 10/2/99, and 2/28/00 sales to GE CAL, and its 11/6/99 sale to GE CAF. *Compare* Department Exs. 1-2 (fourth through seventh assessments identified on NPLs) *with* Taxpayer Exs. 1, 3-5; Tr. pp. 84-84 (Barborka).
21. After the Department came into possession of the 3d party returns, it processed those returns as original returns. Taxpayer Exs 1-5 ("Process as original" handwritten on each 3d party return); Tr. pp. 19-21, 25, 29, 32-33, 35 (Barborka). That means that the Department treated those returns as though ABC had filed them, again, years after the dates on which the transactions reported on those returns occurred. Taxpayer Exs. 1-5; Tr. pp. 19-21, 25, 29, 32-33, 35 (Barborka).
22. Because each ST-556 return bears a unique transaction number (86 Ill. Admin Code § 130.540(b)), when processing the 3d party returns as though ABC filed them, the Department employee processing them was unable to discern that ABC had, in fact, previously filed a separate return regarding four of the transactions described on the 3d party returns. *Compare* Taxpayer Exs. 1, 3-5 (transaction numbers on 3d party returns) *with* Taxpayer Exs. 6-9 (transaction numbers on ABC's returns for same transactions); Tr. pp. 72-75 (Barborka).
23. Even though both Department counsel and the Department employee that testified at Hearing referred to the assessment numbers identified on the NPLs as though those assessments had been reduced to Notices of Tax Liability (NTLs), there was no documentary evidence offered to show that such NTLs were, in fact, prepared and/or issued to ABC after the Department received the 3d party returns in 2003 and 2004.

See Tr. pp. 61-62, 64 (Barborka); *but see* 35 ILCS 120/4.

24. The Department has never asserted in this matter that it determined that the returns ABC actually filed regarding its 6/5/99, 10/2/99, and 2/28/00 sales to GE CAL, and its 11/6/99 sale to GE CAF, were incorrect, or fraudulent.
25. For convenience, the following table identifies the documentary evidence taxpayers offered regarding the assessments identified in the NPLs:

Transaction Number	Assessment number, tax type, and period covered	3d Party ST-556 Return	Vehicle Title Application	Original ST-556 Return
1	000000000000000000 ROT/UT 1999/06	Taxpayer Ex. 2		
2	000000000000000000 ROT/UT 1999/06			
3	000000000000000000 ROT/UT 1999/06			
4	000000000000000000 ROT/UT 1999/06	Taxpayer Ex. 1	Taxpayer Ex. 11	Taxpayer Ex. 9
5	000000000000000000 ROT/UT 1999/10	Taxpayer Ex. 3	Taxpayer Ex. 12	Taxpayer Ex. 8
6	000000000000000000 ROT/UT 1999/11	Taxpayer Ex. 4	Taxpayer Ex. 13	Taxpayer Ex. 7
7	000000000000000000 ROT/UT 2000/02	Taxpayer Ex. 5	Taxpayer Ex. 14	Taxpayer Ex. 6

Conclusions of Law:

When the Department introduced the NPLs into evidence under the certificate of the Director, it presented prima facie proof that John Doe and SJones were personally responsible for ABC's unpaid tax liabilities. 35 ILCS 735/3-7; Branson v. Department of Revenue, 168 Ill. 2d 247, 260, 659 N.E.2d 961, 968 (1995) ("by operation of the statute, proof of the correctness of such penalty, including the willfulness element, is established by the Department's penalty assessment and certified record relating thereto."). The

Department's prima facie case is a rebuttable presumption. Branson, 168 Ill. 2d at 262, 659 N.E.2d at 968. After the Department introduces its prima facie case, the burden shifts to the taxpayer to establish that one or more of the elements of the penalty are lacking. *Id.*

Section 3-7 of the UPIA provides that a personal liability penalty liability may be imposed upon:

- [1] Any officer or employee of any corporation ... who has the control, supervision or responsibility of filing returns and making payment of ... the tax[es] ... imposed ... **and** who willfully:
- [2] fails to file such return **or**
- [3] [fails] to make such payments to the Department **or**
- [4] ... attempts ... in any other manner to evade or defeat the tax

35 **ILCS** 735/3-7(a) (emphasis and brackets added).

The first issue is whether taxpayers were responsible officers of ABC. John Doe and SJones each testified that they were principals of ABC, and that they were responsible for filing its returns, and for making payments of taxes shown due on those returns. Tr. pp. 85-87 (SJones), 111-12, 114 (John Doe). Based on that evidence, I conclude that each taxpayer had the control, supervision or responsibility of filing returns and making payment of taxes imposed by the Retailers' Occupation Tax Act. 35 **ILCS** 735/3-7(a).

The next issue is whether either taxpayer acted willfully. Taxpayers assert that they did not willfully fail to file any returns, or to fail to pay any taxes due regarding the tax assessments the Department asserts remain unpaid by ABC. Tr. pp. 132-34, 136-38 (closing arguments). Illinois case law provides guidance on the issue of willfulness. First, "the Department's prima facie case for a tax penalty presumes willfulness. To rebut

the presumption, the person defending against the penalty must adduce sufficient evidence to disprove willful failure to file returns and pay taxes.” Branson, 168 Ill. 2d at 262, 659 N.E.2d at 968. Whether a responsible officer acts willfully is a mixed question of law and fact. *Id.* at 265, 659 N.E.2d at 970. A responsible officer cannot prove his lack of willfulness simply by denying conscious awareness of a tax deficiency that could have been easily investigated by an inspection of corporate records. *Id.* at 267, 659 N.E.2d at 971.

A concise description of Illinois law regarding willful conduct by a responsible officer was set forth by the appellate court in McLean v. Department of Revenue, 326 Ill. App. 3d 667, 761 N.E.2d 226 (1st Dist. 2001):

Under Illinois law, if a responsible officer uses collected retailers’ occupation taxes to pay other creditors of the corporation, while knowing that he or she was obligated to file the returns and remit the taxes, the “willful” element of section 13½ is satisfied. *Branson*, 168 Ill. 2d at 259, 213 Ill.Dec. 615, 659 N.E.2d at 967; *Estate of Young*, 316 Ill. App. 3d at 378, 248 Ill.Dec. 654, 734 N.E.2d at 953. “A finding of willfulness under section 13½ does not require a showing of actual knowledge of nonpayment. Reckless disregard for obvious or known risks will suffice. [Citation.] If a responsible person in a position to easily discover nonpayment clearly ought to have known of a grave risk of nonpayment but did nothing, a finding of willfulness is justified.” *Estate of Young*, 316 Ill. App. 3d at 375, 248 Ill.Dec. 654, 734 N.E.2d at 952. A corporate officer who is responsible for filing retailers’ occupation tax returns and remitting the collected taxes may not avoid personal liability for tax penalties for nonpayment of such taxes merely by delegating bookkeeping duties to third parties and failing to inspect corporate records or otherwise failing to keep informed of the status of retailers’ occupation tax returns and payments. See *Branson*, 168 Ill. 2d at 267, 213 Ill.Dec. 615, 659 N.E.2d at 971.

McLean, 326 Ill. App. 3d at 675-76, 761 N.E.2d 234-35.

The evidence and arguments taxpayers offered on the question of willfulness involve an identification of the nature of the tax assessments the Department determined was due from, and unpaid by, ABC. The first witness taxpayers called at Hearing was a Department employee. Tr. p. 9. At that time, Department counsel objected, arguing that the judgment in Department of Revenue v. Dombrowski, 202 Ill. App. 3d 1050, 560 N.E.2d 881 (1st Dist. 1990) should be understood to mean that “a taxpayer cannot go into the underlying corporate liability in an officer liability case.” Tr. p. 10. But the Department reads that case too broadly. Dombrowski stands for the proposition that, where the Department properly issues an NTL and a final assessment to a taxpayer, any issues as to the correctness of that final tax deficiency can be challenged only pursuant to the Illinois Administrative Review Act. Dombrowski, 202 Ill. App. 3d at 1053-54, 560 N.E.2d at 883-84 (“Having failed to file such an action, he has instead improperly sought judicial review of the Department’s action as part of his defense to the instant lawsuit; but because of defendant’s failure to comply with the ARA, we are not empowered to review the merits of the Final Assessment or the Revised Final Assessment.”). If the taxpayer fails to appeal the Department’s final assessment, and the Department, thereafter, seeks to collect the unpaid corporate liability from a responsible officer of the corporation, that individual cannot challenge the amount of the final tax deficiency as part of the subsequent collection case. *Id.* at 1054, 560 N.E.2d at 884.

But Dombrowski does not apply here. First, the facts in Dombrowski are not like the facts in this matter. In Dombrowski, there was no dispute that the Department had issued an NTL, and later, a final assessment, to Dombrowski. Dombrowski, 202 Ill. App. 3d at 1054, 560 N.E.2d at 884 (“The Department issued a Final Assessment on October

7, 1974, and defendant does not contend that the Department failed to serve him with notice thereof; consequently, defendant had 35 days from the date of service of the Final Assessment to file an action seeking judicial review of the agency determination. Having failed to file such an action, he has instead improperly sought judicial review of the Department's action as part of his defense to the instant lawsuit; but because of defendant's failure to comply with the ARA, we are not empowered to review the merits of the Final Assessment or the Revised Final Assessment."'). Dombrowski's failure to contest the Department's final assessment pursuant to Illinois' Administrative Review Act acted as a waiver of his right to contest the amount of that unpaid liability when the Department subsequently sought to collect that amount from him personally. But there is no evidence that the Department ever issued an NTL, or separate NTLs, to ABC regarding the assessments that are identified in the NPLs here.

On this point, it is important to recall that not all tax assessments are made following the issuance of a notice of tax liability. 35 **ILCS** 120/4. Some amounts of tax are self-assessed, most often where a taxpayer has filed a return showing an amount of tax due, but for which payment is not made with the filing of the return. In those situations, the Department may issue an NTL, but need not do so. This is made clear by § 4 of the ROTA, which provides, in pertinent part:

* * *

If the tax computed upon the basis of the gross receipts as fixed by the Department is greater than the amount of tax due under the return or returns as filed, the Department shall **(or if the tax or any part thereof that is admitted to be due by a return or returns, whether filed on time or not, is not paid, the Department may)** issue the taxpayer a notice of tax liability

for the amount of tax claimed by the Department to be due, together with a penalty in an amount determined in accordance with Section 3-3 of the Uniform Penalty and Interest Act. ***

35 ILCS 120/4 (emphasis added). At Hearing, Department counsel and the Department employee that testified as a witness frequently referred to the assessments identified in the NPLs as NTLs, but the Department never offered ABC of any NTLs into evidence. Thus, this evidence in this matter is not as clear as was the record in Dombrowski. Dombrowski, 202 Ill. App. 3d at 1054, 560 N.E.2d at 884.

Taxpayers here, moreover, are not attempting what Dombrowski attempted to do. That is, they are not trying to show that a final assessment is incorrect. Rather, they offered evidence, including the testimony of a Department employee, to show that they did not willfully fail to file returns or willfully fail to pay tax due. Some of that evidence described how the assessments arose. That is, taxpayers offered evidence that showed that the Department came into possession of purchaser's cABCes of five returns on which ABC was named as the seller of vehicles, and that the Department thereafter treated those 3d party returns as though they were original returns that ABC filed years after the dates on which the transactions reported on those returns occurred. Taxpayer Exs. 1-5; Tr. pp. 20-21, 25, 29, 32-33, 35, 80-84 (Barborka). The evidence showed that the 3d party returns that formed the bases for four of the tax assessments against ABC that are identified on the NPLs were not, in fact, filed by ABC. *See* Taxpayer Exs. 6-9. Further, the evidence showed that when the Department received the 3d-party returns from someone other than ABC, it was not able to discern whether ABC had, in fact, itself filed returns to report the transactions described in those 3d-party returns. Tr. pp. 72-75

(Barborka); *see also* 86 Ill. Admin. Code § 130.540(b).

The documentary evidence further establishes that four of the five transactions described within the 3d party returns were transactions regarding which ABC had previously filed returns. Taxpayer Exs. 1, 3-9. Each of the four returns that ABC actually filed show no tax due. Taxpayer Exs. 6-9. Taxpayers each testified that the returns filed by ABC regarding those four transactions were correct (Tr. pp. 88-89 (SJones), 112 (John Doe)), and their testimony is corroborated by the returns themselves, each of which reflects that the value of the vehicles reported as having been taken in trade exceeded the gross receipts ABC charged and collected from such sales. Taxpayer Exs. 6-9.

Taxpayers assert that they satisfied whatever statutory responsibilities they had to see to it that ABC file a return regarding each such transaction, and to pay whatever amount of tax was due on those transactions. Tr. pp. 132-34, 136-38 (closing argument). On this point, I note that the Department has never asserted that the assessments identified within the NPLs corrected the returns that ABC proved that it filed regarding the four transactions — indeed, until counsel for taxpayers was retained and asked that administrative subpoenas be issued to the Illinois Secretary of State, the Department did not even know that ABC had, in fact, filed returns regarding those four sales. *See* Tr. pp. 39-40, 127-30 (Barborka). Instead, the Department contends that taxpayers should be found to have acted willfully regarding four 3d party returns that ABC did not file (Tr. p. 128 (Barborka)), and regarding which returns both taxpayers claimed to have no knowledge. Tr. pp. 89-91, 109-10 (SJones), 112-13 (John Doe).

I conclude that taxpayers have offered competent, credible evidence, including documentary evidence that is closely associated with ABC's books and records, to show

that they did not willfully fail to file returns, willfully fail to make tax payments, or willfully attempt to defeat or evade the collection of tax assessed regarding four of the seven assessments identified in the NPLs. Taxpayer Exs. 1, 3-14. Thus, taxpayers have rebutted the presumptive correctness of the Department's determination that they are personally liable for the tax related to assessment numbers 000000000000000000, 000000000000000000,000000000000000000, and 000000000000000000. *See* Department Exs. 1-2; Branson, 168 Ill. 2d at 262, 659 N.E.2d at 968 ("To rebut the presumption, the person defending against the penalty must adduce sufficient evidence to disprove willful failure to file returns and pay taxes.").

While taxpayers offered evidence sufficient to rebut the Department's prima facie case regarding the last four transactions identified on the NPLs, they did not offer similar evidence regarding the three other assessments identified in the NPLs. *See* Department Exs. 1-2. Therefore, taxpayers have not rebutted the prima facie correctness of the Department's determination that they are personally liable for assessment numbers 000000000000000000, 000000000000000000, and 000000000000000000. Branson, 168 Ill. 2d at 262, 659 N.E.2d at 968.

After a taxpayer rebuts the Department's prima facie case, the burden shifts to the Department to prove its case by a preponderance of competent evidence. Novicki v. Department of Finance, 373 Ill. 342, 345-46, 26 N.E.2d 130, 132 (1940). The Department offered no such competent evidence at Hearing. Nor, in response to the credible testimony and documentary evidence taxpayers offered regarding the four transactions for which ABC filed returns, did the Department attempt to show that the original returns ABC filed were incorrect, or why any putative error should be considered

a result of taxpayers' willful acts.

Conclusion:

For the reasons stated above, I recommend that the Director revise the NPL's to eliminate any penalty regarding assessment numbers 000000000000000000, 000000000000000000, 000000000000000000, and 000000000000000000. I recommend that the NPL;s be finalized as so revised, with interest to accrue pursuant to statute.

Date: 8/20/2007

John E. White
Administrative Law Judge